

Message Text

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47

ACTION ARA-20

INFO OCT-01 ISO-00 AID-20 CIAE-00 EB-11 FRB-03 INR-11

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LAB-06 SIL-01 OMB-01 NSC-07 SS-20 STR-08 CEA-02 COM-08

L-03 PA-04 PRS-01 USIA-15 H-03 DRC-01 /172 W

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P R 141500Z SEP 74

FM AMEMBASSY BRASILIA

TO SECSTATE WASHDC PRIORITY 5600

INFO AMCONSUL RIO DE JANEIRO

AMCONSUL SAO PAULO

UNCLAS BRASILIA 7050

D.O. 11652: N/A

TAGS: EFIN, BR

SUBJECT: BRAZIL REDUCES TERMS ON FOREIGN FINANCIAL LOANS

1. THE NATIONAL MONETARY COUNCIL REDUCED EFFECTIVE TODAY (SEPT 14) THE MINIMUM REPAYMENT TERMS ON FOREIGN FINANCIAL LOANS TO FIVE YEARS FROM TEN YEARS. IT ALSO REDUCED TO EIGHT YEARS FROM TWELVE YEARS THE MINIMUM TERMS FOR FINANCIAL LOANS TO BE EXEMPTED FROM THE 25 PERCENT WITHHOLDING TAX ON THE GROSS INTEREST REMITTED ABROAD. THE NEW TERMS APPLY TO BOTH RESOLUTION 63 LOANS (FOREIGN CURRENCY LOANS CONTRACTED THROUGH A LOCAL INTERMEDIARY) AND LAW 4131 LOANS (FOREIGN CURRENCY LOANS CONTRACTED DIRECTLY BY LOCAL BORROWER WITH FOREIGN LENDERS).

2. COMMENT: THIS MOVE CAME AS NO SURPRISE AS IT HAD BEEN PREDICTED FOR SOME TIME (BRASILIA 5585). AS THE REPAYMENT TERMS ON EURODOLLAR CREDITS HAVE BEEN DECREASING IN RECENT MONTHS, IT BECAME INCREASINGLY DIFFICULT FOR BRAZIL TO CONTRACT FUNDS AT A MINIMUM OF TEN YEARS. WHILE, FROM THE STANDPOINT OF PRUDENT FOREIGN DEBT MANAGEMENT, THE AUTHORITIES HAD BEEN HOPEFUL THEY COULD MAINTAIN THE TEN-YEAR TERMS, THEY COULD

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NOT POSSIBLY STICK FOR VERY LONG WITH A POLICY WHICH WAS

CONTRARY TO THE REALITIES OF THE INTERNATIONAL MONEY MARKET. STAYING WITH THIS POLICY AS LONG AS IT DID, BRAZIL DID GET SOME BENEFITS THIS YEAR. DURING THE FIRST HALF, IT RECEIVED \$2,808 MILLION IN FOREIGN FINANCIAL LOANS ON TEN-YEAR TERMS. THESE FUNDS, ALONG WITH ABOUT \$500 MILLION IN FOREIGN DIRECT INVESTMENTS, WERE SUFFICIENT TO COVER THE CURRENT ACCOUNT DEFICIT WITHOUT DIPPING INTO RESERVES, WHICH AT THE END OF JUNE WERE AT THE SAME LEVEL AS DECEMBER 1973, I.E., \$6.4 BILLION. THE INFLOW OF FOREIGN FUNDS THROUGH FINANCIAL LOANS, HOWEVER, SLOWED DOWN DURING AUGUST AND SEPTEMBER. FOR THIS TWO-MONTH PERIOD BRAZIL RECEIVED, ACCORDING TO THE CENTRAL BANK ANNOUNCEMENT, ONLY \$810 MILLION, WHICH WAS SOMEWHAT BELOW THE AVERAGE MONTHLY INFLOW OF THE FIRST SIX MONTHS. THE AUTHORITIES WERE THUS FORCED TO REDUCE THE TERMS ON FINANCIAL LOANS HOPING THAT THEY WOULD BE ABLE TO RECEIVE ENOUGH FOREIGN CAPITAL DURING THE REST OF THE YEAR SO AS TO AVOID A SIGNIFICANT REDUCTION IN THEIR RESERVES, WHICH AT THE END OF AUGUST HAD ALREADY DROPPED TO \$6,119 MILLION. MONETARY AUTHORITIES HAVE ALWAYS CONSIDERED THEIR RESERVE HOLDINGS A KIND OF SAFETY VALVE TO BE TURNED ON ONLY IN CASES OF REAL EMERGENCIES (SEE BRASILIA 6926). IT WAS, THEREFORE, TO BE EXPECTED THAT THE AUTHORITIES WOULD REDUCE THE TERMS ON FINANCIAL LOANS -- THUS MAKING LENDING TO BRAZIL MORE ATTRACTIVE--BEFORE PERMITTING A SIGNIFICANT DECREASE IN THEIR OFFICIAL RESERVE HOLDINGS.

CRIMMINS

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